Supreme Court, U.S.
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No. 90-710

In The

Supreme Court of the United States

October Term, 1990

ST. PAUL FIRE AND MARINE INSURANCE COMPANY,

Petitioner,

vs.

SUPERIOR COURT FOR THE STATE OF CALIFORNIA FOR THE CITY AND COUNTY OF SAN FRANCISCO,

Respondent.

Petition For Writ Of Certiorari To The Supreme Court Of California

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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ARGUMENT

I

THE CALIFORNIA STATE COURTS HAVE JURISDICTION OVER THE SUBJECT MATTER OF THE ACTION

Implicit in the argument of St. Paul Fire and Marine Insurance (hereinafter referred to as St. PAUL), and stated explicitly in its "Questions Presented for Review" are the false premises that this suit is instituted under the Miller Act, 40 U.S.C. §270a et seq., and that the Plaintiffs are seeking to recover benefits under a bond. This action is not instituted under the Miller Act and the Plaintiffs are not seeking to recover benefits under a bond. Rather they are seeking to recover damages through state court causes of action for breach of contract; breach of covenant of good faith and fair dealing, and fraud and conspiracy to defraud. The damages sought by those causes of action are clearly not, as St. PAUL contends, the same as those that would flow from an action on a bond. The authorities agree that such state causes of action are separate and distinct from a Miller Act claim against a surety.

In the recent case of *K-W Industries v. National Surety Company*, (9th Cir. 1988) 855 Fed. 2d 640, K-W Industries (hereinafter "K-W"), the subcontractor, made a claim for payment against the surety on a Miller Act bond. When the surety refused to pay the claim K-W brought an action on the bond in the United States District court.

K-W then also instituted a separate action in the state court alleging that the surety acted in bad-faith in refusing to pay its claim, whereupon the surety removed the

action to the federal court on the basis of diversity jurisdiction. The district court then *sua sponte* dismissed the action for lack of subject matter jurisdiction.

In so dismissing the case the district court reasoned that although K-W plead its claim against the surety as founded upon state law, the claim was properly characterized as a federal claim predicated on the rights conferred upon K-W by the Miller Act. Applying law which has now been superseded, the court reasoned further that as the federal court's removal jurisdiction is derivative, the state court's lack of jurisdiction also deprived the federal court of jurisdiction.

On appeal, the surety argued that state law subjecting sureties to tort liability for bad faith insurance practices conflicted with the purposes of the Miller Act, one of which was to protect Miller Act sureties from diverse state regulation, and that the application of state bad-faith laws were thus preempted. The court, however, disagreed:

> 'The purpose of the Miller Act "is to protect persons supplying materials and labor for federal projects." *United States ex rel. Martin Steel Constructors, Inc. v. Avanti Constructors, Inc.*, 750 F.2d 759, 761 (9th Cir. 1984), cert. denied, 474 U.S. 817, 106 S.Ct. 60, 88 LEd 2d. 49 (1985).' [pp. 642, 643].

The court went on to hold that:

> 'We agree with the tenth circuit's observation that the Miller Act, like the mechanic's lien it replaces, "is not the exclusive remedy in regard to the obligation which such lien secures," but rather, "is 'separate from and independent of any *in personam* rights . . . which the supplier

> might have against the owner, a contractor, or subcontractor, by way of a contract or otherwise.' " *United States ex rel. Sunworks Division of Sun Collector Corp. v. Insurance Company of North America*, 695 F. 2d 455, 458 (10th Cir. 1982) (quoting *In re Scherer Hardware & Supply, Inc.*, 9 B.R. 125, 130 (N.D. ILL. 1981). For the purpose of preemption analysis, we see no reason to distinguish between remedies that a supplier may have against an owner, contractor, or subcontractor as opposed to a surety.'
>
> [. . .]
>
> **"because K-W's action arises under state law, not under the Miller Act, the [. . .] state court in which this action was originally filed has subject matter jurisdiction.** The district court thus erred in dismissing the action for lack of removal jurisdiction." [pp. 643, 644]. [Bold emphasis added].

In the similar case of *Alvarez v. Insurance Company of North America*, (1987 N.D. Cal.) 667 F. Supp. 689, the plaintiff was a subcontractor to Feinstein Construction, the bonded general contractor (coincidentally the same contractor as in the present case). The Insurance Company of North America (hereinafter "INA") issued the Miller Act Bond covering the project. The plaintiff sued Feinstein and INA in federal court both to recover under the Miller Act bond and for bad faith under California law. The bad faith action was dismissed on the ground that such relief was not available under the Miller Act.

After an arbitration award and in response to the large number of claims on the Feinstein bond INA filed an interpleader action, depositing the amount of the bond. Having recovered only a pro rata share of its claim

under the bond the plaintiff then reasserted its bad faith claim in the Superior Court of California.

INA then removed the action to federal court on diversity grounds where it argued that a Miller Act surety is not subject to regulation under the California Insurance code and that the state insurance regulations were preempted by the Miller Act. The court found otherwise holding that:

> "Allowing a bad faith suit outside of the Miller Act does not interfere with the desired uniformity of remedy *under* the Act. Nor does a congressional purpose of providing a uniform remedy imply that such a remedy was to be exclusive." [p. 693].
>
> "In this case, [the plaintiff] has brought a separate action for unfair insurance practices under state statute. In other words, rather than asking this court to expand the federal remedy, plaintiff brings an additional but separate state claim." [p. 694].
>
> "The operation of the Miller Act and various authorities support the conclusion that the Miller Act does not totally occupy the field. For example, a Miller Act suit on the surety bond is not a subcontractor's exclusive remedy." [p. 695 citations omitted].

The foregoing authorities make an absolute distinction between actions on the bond and the additional but separate state court remedies which the respondents have plead in this action. The Court's attention is also drawn to the fact that the action on the bond was determined by an arbitrator outside both the state and federal court systems and not, as St. PAUL contends on page 10 of its Petition, "in federal Court".

II

ALTHOUGH PETITIONER MAY BE ESTOPPED IN FEDERAL COURT FROM ASSERTING THE STATUTE OF LIMITATIONS ON THE MILLER ACT BOND THE STATE COURT IS NOT THEREBY DIVESTED OF JURISDICTION OVER THE STATE CAUSES OF ACTION

St. PAUL does not appreciate that the damages which flow from its breach of contract are not identical to the benefits under the Miller Act bond and that the suit is not "on the bond", as discussed above. Nor does it appreciate that the Plaintiffs are not asserting an estoppel argument in such an action but rather their separate and independent *in personam* rights. On page 8 of the Petition, St. PAUL has cited the cases of *United States for the Use of E.E. Black Limited v. Price MacNamar Construction Co.*, (9th Cir. 1963) 320 F.2d 663; *United States for the Use of Nelson v. Reliance Insurance Co.*, (10th Cir. 1971) 436 F.2d 1366 and *United States for the Use of Texas Bitulithic Co. v. Fidelity and Deposit Co. of Maryland*, (5th Cir. 1987). These authorities indicate that the federal court will retain jurisdiction over an action instituted under 40 USC §270(b) on a Miller Act bond where there is an indication that a surety may be estopped from asserting the statute of limitations. They do not indicate, however, and neither does it follow, that exclusive jurisdiction over the state causes of action is thereby conferred upon the federal court, as would appear to be implicitly contended by St. PAUL.

III

THE COMPUTATION OF THE LIMITATION PERIOD UNDER 40 USC §270(b) IS NOT AN ISSUE BEFORE THE CALIFORNIA STATE COURTS

On page 9 of its Petition, St. PAUL contends that the statute of limitations in 40 USC §270(b) is a federal statute of limitations and that the computation of the limitations period, including what will toll it, is a question of federal law. There is, however, no dispute between Plaintiffs and St. PAUL in this regard so that the issue is not one before the state courts.

The Plaintiffs have made no allegations concerning the computation of the limitation period nor that it is tolled. A contract not to assert a statute of limitations defense is breached by the assertion of such a defense, whensoever asserted. The computation of the limitation period will be of no relevance, therefore, to the state court's consideration of St. PAUL's breach of contract.

IV

THE EXISTENCE OF A MILLER ACT BOND IS NOT AN ISSUE BEFORE THE CALIFORNIA STATE COURTS

Contrary to the assertions of St. PAUL, the Plaintiffs will not even have to prove the existence of a Miller Act bond as St. PAUL, itself, has consistently averred the existence of such a bond. (See declaration of Bruce Reed in support of St. PAUL's Motion to Dismiss for Lack of Subject Matter Jurisdiction, attached hereto as Exhibit 1). The question as to the existence of the bond will not, therefore, be considered by the state court.

V

HAVING WAIVED ITS RIGHT TO REQUEST REMOVAL TO FEDERAL COURT THE PETITIONER CANNOT BE PERMITTED TO CONTEND THAT THE STATE COURT LACKS JURISDICTION

The federal courts previously followed the "derivative jurisdiction rule" which provided that where the state court had no subject matter jurisdiction because the claim was within the exclusive federal jurisdiction, the federal court to which the action was removed could derive none. (*Emrich v. Touche Ross & Co.*, (9th Cir. 1988) 846 F.2d 1190). The "derivative jurisdiction" rule was eliminated in 1986. 28 USC §1441(e) now provides that removal jurisdiction "is not precluded [. . .] because the state court from which such civil action is removed did not have jurisdiction over the claim." The rule now only applies to state court actions filed before its enactment on June 19, 1986. (*Emrich v. Touche Ross & Co., supra*). In the transcript of the Superior Court proceedings of March 29, 1990 at page 3, lines 18-19, counsel for the Petitioner can be seen to be under the mistaken impression that the "derivative jurisdiction" rule is applicable to this action. The present action was commenced on June 24, 1986 by the filing of the Complaint in the California Superior Court (and process was served some time later) so that the "derivative jurisdiction" rule is not applicable. If, as St. PAUL contends, there is federal jurisdiction over this action it would not, therefore, have been precluded from removing the action to federal court.

A defendant waives the right to removal and submits to state court jurisdiction if it fails to file a notice of removal within 30 days after receipt of the first pleading

in the state action that sets forth a removable claim. (28 USC §1446(b)). St. PAUL has thus submitted to the jurisdiction of the California state courts.

The Petitioner contends, on page 9 of the Petition, that it did not waive its jurisdictional objection by failure to remove to federal court as jurisdiction cannot be conferred by waiver. While it is agreed that jurisdiction is not *conferred* by waiver this is clearly not the same as a submission to jurisdiction. The fact remains that St. PAUL, by its failure to file the required notice of removal under 28 USC §1446(b), has, by waiver, submitted to state court jurisdiction. To hold otherwise would be to render the provisions of this section without effect. St. PAUL's submission to the state court's jurisdiction has, therefore, rendered moot its subsequent protestations thereto.

In its "Statement of the Case", St. PAUL has falsely accused the Respondents of "artful pleading". Notwithstanding, this would not affect the Petitioner's submission to state court jurisdiction by its failure to timely remove. In *Cantrell v. Great Republic Insurance Co.*, (9th Cir. 1989) 873 F.2d 1249, where the defendant could have known that the plaintiff's state claims were preempted by ERISA, notwithstanding the plaintiff's "artful pleading", the rule requiring removal within 30 days following receipt of the original complaint was enforced.

VI

THE COMPLAINT STATES NO CLAIM OVER WHICH THE FEDERAL COURTS HAVE JURISDICTION

As discussed above, the federal courts have exclusive jurisdiction over a claim on a Miller Act bond only when

the action is directly "on the bond". The latter two causes of action of the Complaint are premised on the first cause of action and not, as the St. PAUL alleges, on a claim payable under a bond. The Court's attention is drawn to page 10 of St. PAUL's Argument wherein it contends that paragraphs 20 and 25, and paragraphs 33 and 38, of the second and third causes of action respectively of the Second Amended Complaint are premised upon the plaintiffs having a valid claim under a bond. An examination of these paragraphs will reveal, however, that they are not so premised and that only state causes of action are being plead.

Because only state causes of action are being plead there is no claim over which the federal courts are able to independently acquire jurisdiction. (*Hunter v. United Van Lines*, (9th Cir. 1984) 746 F.2d 645, 649; *Aragon v. Federated Department Stores, Inc.*, (9th Cir. 1986) 750 F.2d 1447, 1457). It follows that the state courts not only have jurisdiction over the causes of action plead but that their jurisdiction is exclusive.

VII

CONCLUSION

St. PAUL's arguments are predicated upon the false premise that the action is instituted under Section 270(b) of the Miller Act (40 USC §270(b)). The authorities clearly distinguish between the non-exclusive remedy of an action instituted under 40 USC §270(b) and the independent state court proceedings of which the present action is but one example.

Even if the filing of the action in state court was incorrect, St. PAUL would, by its failure to file a timely notice of removal, have waived its right to assert federal jurisdiction and have submitted to state court jurisdiction. By their nature, the state causes of action are distinct from a claim instituted under the provisions of 40 USC §270(b) and are not, therefore, conclusive of a federal issue. Even if they were, St. PAUL's failure to file its notice of removal has ensured that there will be no conflicting outcome in federal court.

As argued, the state courts have exclusive jurisdiction over the causes of action plead. To grant St. PAUL's Petition would be to deny to the Plaintiffs a forum through which their grievances may be redressed. It is in the interests of justice and in accordance with established law that the Petition be denied.

Dated: November 30, 1990

Respectfully submitted,
WILLIAMS & MARTINET

By /s/ Michael J. Guglielmino
MICHAEL J. GUGLIELMINO
Attorneys for Plaintiffs and Real Parties in interest

APPENDIX

FREDERICK W. FLOWERS, ESQ.
PETER V. SHACKTER, ESQ.
MARK P. GRUNDMAN, ESQ.
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San Francisco, California 94111
Telephone: (415) 981-5130

Attorneys for Defendant
ST. PAUL FIRE & MARINE INSURANCE COMPANY

SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF SAN FRANCISCO

JAMES LEE JONES; GEORGE EDWARD WESSON; FAR WEST PAINTING AND CONSTRUCTION; and PERCELL-JONES CONSTRUCTION, Plaintiffs, vs. ST. PAUL FIRE AND MARINE INSURANCE COMPANY; and DOES 1 TO 100, inclusive, Defendant.	CASE NO. 860 196 REPLY DECLARATION OF BRUCE REED (Filed Jan, 29, 1990) Date: February 1, 1990 Time: 9:30 a.m. Place: Department 9 Trial Date: None Set

I, BRUCE REED, declare:

1. Reference is made to my declaration filed herein on December 27, 1989. I am the same declarant and I hereby incorporate said declaration by reference.

2. Attached hereto marked Exhibit "A" and hereby incorporated by reference is a true copy of a notice of bond amendment or cancellation with regard to bond number 400GW6738.

3. The purpose of the document is to show an addition to the face amount of the bond.

4. It is the regular course of business for the San Francisco office of St. Paul Fire and Marine Insurance to issue a notice of bond amendment when the face amount of a bond is in fact amended and to keep it in the file to memorialize the fact of the amendment.

5. The present notice of bond amendment was in fact so made by the San Francisco office and so kept in its file in the regular course of business.

6. On the right hand side of the document, in a space indicated "class code" appears the number 330.

7. Of my personal knowledge "330" indicates various types of construction bonds on public words owned by the United States of America and issued pursuant to the Miller Act, 40 U.S. Code §270 *et seq.*

8. Attached hereto as Exhibit "B" is a true copy of our file copy of a letter with enclosures in our file regarding a claim by Far West Paint and Construction and George Weston against bond 400GW6738.

9. Mr. Ron Mund the addressee of the letter, is of my personal knowledge, is in the bond claims department of St. Paul Fire and Marine Insurance Company in St. Paul, Minnessota.

10. J. W. Gilliland works in my office as bond field supervisor. I am familiar with Mr. Gilliland's handwriting and pages 1 and 4 of the documents appeared to be in his handwriting.

11. Of my personal knowledge, Mr. Wesson and one other man were in our office on or about February 8, 1989, and spoke with Mr. Gilliland about a claim.

12. It was the regular course of business of the San Francisco branch office to transmit to the claims department of the home office, in writing, any bond claims submitted to it and to file copies thereof as a record of the transmission and the documents comprising Exhibit "B" were in fact transmitted to the home office and a copy kept in the file in the regular course of business.

I declare under penalty or perjury under the laws of the State of California that the foregoing is true and correct.

This declaration was executed on the 26th day of January, 1990, at San Francisco, California.

/s/ Bruce Reed
Bruce Reed

EXHIBIT A

Property & Liability Insurance

NOTICE OF BOND AMENDMENT OR CANCELLATION

TYPE OF BOND (C) BOND NO. 400 GW 6738

PRINCIPAL: Feinstein Construction, Inc. and Neil D. Feinstein, Contractor

ADDRESS AND ZIP CODE:

OBLIGEE: U.S. Navy

ADDRESS AND ZIP CODE:

AGENCY NAME, ADDRESS & ZIP: R. L. Milsner, 2775 Mitchell Drive, Suite 211, Walnut Creek, CA 94598

AGENCY NUMBER: 045045

FORM OF COVERAGE (Fid. only):

MAJOR GROUP CODE:

METHOD: A. Continues Indefinitely; B. Expires Definitely - Use Renewal Cert.; C. Expires Definitely - New Bond Required; D. Term Bond - Term Premium; E. H.O. Responsibility

CLASS CODE (All Bonds): 330

DATE OF CHANGE: 8/19/85

PREMIUM PERIOD: FROM 3/16/84 TO 3/16/85

COMMISSION: 30%

FOR CONTRACT ONLY: ☐ Bond ☒ Min.

TYPE OF CONTRACT (Contract only): 4

SUPPLEMENTAL QUESTIONNAIRE

TRANSACTION DESCRIPTION

To Bill Overrun:
Final: 1,539,261.00
Orig.: 1,374,504.00
Over: 164,757.00
Rate: 5.25
A.P.: 865.00

ST. PAUL FIRE & MARINE INS. CO.
NO. CALIF. SERVICE CENTER
AUG 23 1985
JOHN W. DAVIS
BOND MANAGER
SAN FRANCISCO BRANCH OFFICE

1. Financial Folder
2. Original Eff. Date
3. Issuer: A ☐ C ☐ D ☒ 4. M/P Yes ☐ No ☐
5. Dur's No. 6. SIC 1542
7. Prem'l-Flat ☐ Short ☐ Pro-Rate ☐

ORIGINAL BOND/CONTRACT AMOUNT	AMOUNT CANCELLED	RETURN PREMIUM	AMOUNT ADDED	ADDITIONAL PREMIUM	REVISED BOND Size Code AMOUNT	REVISED BOND PREMIUM
1,374,504.00	ST. PAUL FIRE & MARINE INS. CO. NO. CALIF. SERVICE CENTER AUG 19 1985 THERESA L. GROSHONG, Bond Dept. SAN FRANCISCO BRANCH OFFICE		164,757.00	865.00	1,539,261.00	

13037 Rev. 8-81 Printed in U.S.A.

SERVICE CENTER COPY

BEST AVAILABLE COPY

EXHIBIT B

OFFICE MEMO

The St Paul

Date _____

From ST. PAUL FIRE & MARINE INS. CO. NO. CALIF. SERVICE CENTER

Dept. FEB 8 1989

Office JOHN GILLILAND, Bond Field Sup. SAN FRANCISCO BRANCH OFFICE

Address _____

TO: RON MUND
BOND CLAIMS

RE: FEINSTEIN CONSTRUCTION 400GW6738

Dear Ron,

George Wesson from Far West Printing & Construction came into our office today to make a claim on 400GW6738. He will be calling you in the morning about it.

Attached are the papers he left with me. He also indicated that the problems with the Navy and Davis-Bacon have been cleared up. Nancy Hernandez at San Bruno Navel Construction Facility has more information – I don't have a phone number.

The phone number for George Wesson is 453-9176.

/s/ John Gilliland

Sharada
CONSTRUCTION, INC.
LICENSED CONTRACTOR

June 12, 1986

Mr. G. William Tischer
The Tischer Company
201 Sansome Street
San Francisco, CA 94104

Dear Fellow BOMA Member:

Sharada Construction, Inc., as a new allied member, would like to introduce ourselves.

Knowing the quality that BOMA members expect, we would like to assist you with your building projects starting from the permit stage through the completion of the construction. Sharada Construction is a lean, innovative competitor in the construction industry specializing in commercial remodeling, tenant improvements, historical renovations, as well as, seismic upgrades. With this approach, our staff has achieved $6 million in business in the first half of 1986.

As our client, you can expect principal involvement and leadership in every project – unsurpassed quality assurance. We are looking forward to meeting and assisting you with any construction needs you may have.

Sincerely,

SHARADA CORPORATION, INC.

/s/ Neil D Feinstein
Neil D. Feinstein
President

NDF/mm

415•641•1792
3221 TWENTIETH STREET
SAN FRANCISCO
CALIFORNIA
94110

Grady Newberry
c/o St. Paul Fire and Marine Ins.
201 – 3rd Street
San Francisco – CA 94103

June 25, 1984.

Re: Bond #400GW6738 Feinstein Construction, Inc.

Dear Mr. Newberry:

The office of the contracting officer, located at the Concord Navel Weapons Station in Concord, California, has directed the undersigned to you for payment out of Bond #400GW6738 Feinstein Construction, Inc., as and for the following reasons:

As Subcontractor under said Feinstein's contract with the United States Navy, contract #N62474-82-C-D348, the undersigned did a demolition job on Bldg. IA-10 at said Concord Naval Weapons Station for Feinstein Construction, Inc.

Although the job has been completed and the United States Navy is totally satisfied with same; and although Feinstein has been invoiced and presented with said invoices by the undersigned, said Feinstein, even though they have themselves billed the United States Navy for said demolition job, has willfully failed, neglected and refused to pay the undersigned the sum of $68,000.00

which represents that amount still due and owing on said demolition job.

Enclosed herewith, and hopefully to expedite this matter, are the heretofore mentioned invoices.

Taking all of the aforesaid into consideration, NOTICE IS HEREBY GIVEN that the undersigned is herein making a formal request upon you for payment in the amount of $68,000.00 out of Bond #400GW6738 Feinstein Construction, Inc.

Thank you for your consideration and co-operation,

/s/ George Wesson

SHARADA

400GW6738

CONCORD NAVAL WEAPONS STATION
N62474-82-C-D348

FAR WEST CONSTRUCTION

Demand Two Years Ago

4-03-84 Origional Contract
68,000 + Claim.

George Wesson FAR WEST Painting & Construction.

453-9176

Nancy Hernandez, Head of Labor Relation US Navy, San Bruno Naval Construction Facility Problems with U.S.

Navy and Davis-Bacon are resolved – proof available upon demand.

Any problem related to Daniel West and workers comp. are resolved.